Commonwealth of Massachusetts
State Ethics Commission

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PUBLIC ENFORCEMENT LETTER 97-3

Dear Mr. Murphy:

As you know, the State Ethics Commission has conducted a preliminary inquiry into allegations that as executive director of the Massachusetts Health and Education Facilities Authority ("HEFA"), you violated G.L. c. 268A by accepting items of substantial value from Goldman, Sachs & Co. ("Goldman Sachs"). Based on the staff's investigation (discussed below), the Commission voted on January 15, 1997, to find that there is reasonable cause to believe that you violated G.L. c. 268A, §§3(b) and 23(b)(3). In view of certain mitigating circumstances (also discussed below), the Commission, however, has determined that further proceedings are not warranted. Rather, the Commission has concluded that the public interest would be better served by disclosing the facts revealed during our inquiry and explaining applicable provisions of the law, with the expectation that this will insure both your and other state employees' future understanding of and compliance with the conflict law. By agreeing to this public letter as a final resolution of this matter, you do not admit to the facts and law discussed below. The Commission and you have agreed that there will be no formal action against you, and that you have chosen not to exercise your right to a hearing before the Commission.

I. Facts

1. HEFA, an independent state authority, was created by special legislation in 1968. *St. 1968, c. 614.* HEFA provides an alternative market mechanism through which hospitals, schools, and other institutions serving the public's health, educational and cultural needs can borrow money. Thus, HEFA provides capital financing to public and non-profit institutions for higher education, non-profit hospitals, nursing homes and their affiliates, non-profit research and cultural institutions, and schools for the handicapped. This financing is accomplished primarily through HEFA issuing tax-exempt bonds. The monies raised are used for project acquisitions, construction, renovation, refinancing and equipment financing.

HEFA is not state funded. Instead, HEFA derives its operating funds from fees generated from the financial services it provides to participating institutions. In this regard, it competes in the marketplace with other tax exempt bond-issuing sources such as the Massachusetts Industrial Finance Authority ("MIFA") and local industrial finance authorities; with federal agencies, most notably the Federal Housing Administration of the United States Department of Housing and Urban Development;[1] with non-exempt sources and other traditional means of financing for clients. HEFA is different from bonding issuers like the Massachusetts Treasurer in that it is a "conduit" issuer; the revenues behind its bonds are the revenues of the borrowing institution, not HEFA's or the Commonwealth's revenues.[2]

2. From May 1989 to June 1995, you were HEFA's executive director. As executive director, you had official responsibility for all of HEFA's actions. For example, you assigned the HEFA staff who would work with a borrowing institution in developing a bond proposal. Once the proposal was developed, it was presented to the HEFA board of directors for approval. You assigned HEFA staff to make the bond presentation to the HEFA board of directors. You also approved all agenda items for board meetings. After the HEFA board acted, you

typically participated in pricing the bond.[3]

3. Goldman Sachs, a New York limited partnership, is an investment banking and securities firm with headquarters in New York City. At the end of 1995, Goldman Sachs' assets totaled slightly over $1 billion.

4. For a number of years, including the years in which you served as HEFA executive director, Goldman Sachs has been a leading underwriter of bonds for non-profit institutions in Massachusetts. As an underwriter, Goldman Sachs tests the market for a bond, establishes a price for the bond, and then agrees to sell all or part of the bond issue at that price.

5. During your tenure at HEFA, Benjamin Wolfe ("Wolfe") was a Goldman Sachs vice president within the firm's Municipal Bond Department and was one of Goldman Sachs' senior investment bankers for non-profit institutions in Massachusetts.[4]

6. Between 1989 and 1995, HEFA issued approximately $6.4 billion in tax-exempt bonds. Some bonds are issued for new construction, in which case HEFA would receive the proceeds of the sale of the bonds, provide for the payment of the costs of the issue, such as attorneys' fees pursuant to a pre-approved schedule, and remit funds to the institution upon the receipt of a requisition and pursuant to a pre-approved project description. On refinancing issuances, HEFA might receive funds constructively, through a bank trustee, for instance, which would hold funds in escrow, and make the payment contemplated by the pre-approved schedule.

7. Goldman Sachs was the lead underwriter for approximately 25 percent of the $6.4 billion in bonds issued by HEFA between 1989 and 1995. Goldman Sachs earned commissions of several million dollars on these bonds.

8. HEFA reserves the right not to enter into a bond transaction with a particular underwriter if it does not wish to do so. This power was not exercised during your tenure, however.

9. In addition to tax-exempt bond financing, HEFA also agrees to support "pools," transactions where one or more borrowers finance two or more projects or needs through a single umbrella bond issue. In 1991, HEFA entered into a "pool" with a Massachusetts hospital which was a Goldman Sachs client. Goldman Sachs was chosen to manage the pool, a bonding of approximately $30 million.

10. In 1991 or 1992, HEFA issued a Request For Proposals ("RFP") for a short-term investment manager for its bond proceeds. Goldman Sachs submitted a bid, but was not chosen. In 1994, HEFA was choosing a re-marketing agent to replace a pool for a firm that was no longer involved in that type of business. HEFA issued an RFP for a manager for the pool. Goldman Sachs submitted a bid, but again was not selected.

11. As HEFA executive director, you participated in each of the foregoing decisions regarding which firm would be selected as HEFA's short-term investment and pool managers.

12. On the following three occasions Wolfe provided you with entertainment where your pro rata share cost $50 or more:

> (a) a July 19, 1990 dinner at Cafe Budapest in Boston, attended by you, Mrs. Murphy, Wolfe and Mrs. Wolfe. The total cost for the dinner was $284.30; your pro rata share for you and your wife was $142.15;
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> (b) a November 20, 1992 dinner at Le Bernadin Restaurant in New York City, NY, and theater tickets to "Phantom of the Opera," for you, Mrs. Murphy, Wolfe and Mrs. Wolfe. The total cost was $735; your pro rata share for you and your wife was $367.50; and
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> (c) an October 23, 1993 dinner at Christopher's Restaurant in Phoenix, AZ, attended by you, Mrs. Murphy, Wolfe and Mrs. Wolfe and two other couples. The total cost for the entertainment was $482.86; Your pro rata share for you and your wife was $120.72.

13. Goldman Sachs reimbursed Wolfe for the above expenses incurred in entertaining you. Goldman Sachs viewed the expenses as business expenses warranting reimbursement. As described above, Goldman Sachs, through Wolfe, provided you with a total of approximately $630 in gratuities based on you and your wife's pro rata share.

14. According to your testimony, you met Wolfe in 1989 shortly after you became HEFA's executive director. Your first conversation with Wolfe took place by telephone regarding a controversy involving a number of HEFA clients leaving HEFA to obtain their funding through MIFA, which at that time was competing with HEFA in financing bonds for schools and hospitals. You wanted to understand Wolfe's perspective, as his company was lead underwriter on a number of deals and had been blamed by many at HEFA for the loss of business to MIFA. You also wanted to repair relations with Wolfe, if possible, because HEFA wanted to regain many of the Goldman Sachs clients it had lost to MIFA.

Your first opportunity to work with Wolfe on a bond issue took place in the summer of 1989 on a hospital transaction. Goldman Sachs was the lead underwriter on the bond issue. Because it was your first opportunity to rectify HEFA's problems (created by its competition with MIFA), you took a more active role in this bond issue. You and Wolfe came to know each other as you worked together on this transaction. You began to develop a great deal of respect for Wolfe's professionalism. Wolfe was helpful in offering advice to you because Wolfe had held a similar executive director position in Illinois and had a number of insightful tips for you. Goldman Sachs, through Wolfe, could have been involved in as many as a dozen HEFA transactions during a peak year in your tenure. HEFA typically was involved in 25 to 35 transactions per year during that period.

You saw Wolfe approximately twice a week between 1989 and 1995. Wolfe frequently ate lunch at HEFA's office, paid for by HEFA. At least once a month, you and Wolfe would leave the office and go out to lunch together and you would often charge the expense to HEFA. These occasions were related to work being done on bond issuances.

In about 1990, you and Wolfe began to socialize in a non-business atmosphere and develop a personal relationship. You and Wolfe had a number of things in common, such as past job experiences and children of common ages. In 1990, Wolfe's wife, whom you had previously met, had an opportunity to be in Boston to visit their daughter, a Boston University student, and the Wolfes got together with you and your wife for dinner at Cafe Budapest as described above. This sort of gathering did not take place often because Wolfe's wife was rarely in Boston, and you and your wife were not in New York very often. Whenever the occasion presented itself, the two couples would try to get together.

You and Wolfe took turns creating social opportunities, and would try to include your spouses or members of your families.[5/] A typical gathering of the two families took place during a Goldman Sachs health care conference in Orlando, Florida in 1992. You rented a boat using personal funds and invited Wolfe, his wife and daughter. Two of your four children were also present. (You could not recall any such outing in a non-conference related setting.) You thought of these occasions as separate from routine business contacts with Wolfe. In your view, they were social and personal gatherings at which either Wolfe or you would pay. In the instances where you paid, you used your personal credit card, not HEFA funds. In the instances where Wolfe paid, you had no knowledge as to how Wolfe paid. To the extent you thought about it, your assumption would have been that Wolfe paid personally, not through Goldman Sachs. As to those occasions where Wolfe paid, you never reflected on whether the cost was greater than $50 for you and your spouse, but you assumed that it was. Regardless of who paid, there was no business discussed; on these occasions topics included family life and personal interests. While your main motivation for the gatherings was personal, you also saw these dinners with Wolfe as a way to help HEFA form a relationship with Goldman Sachs.

You pointed out that in addition to the boat outing, there were other occasions where you paid with your own personal credit card to entertain Wolfe. For example, on October 18, 1990, you and your spouse treated the Wolfes to dinner in New York City at Orso Restaurant. You personally paid $177.80 for the meal. On July 27, 1994, you treated Wolfe to dinner at Toscano Restaurant in Boston. You paid $121.05 for the meal, during which you sought Wolfe's advice pertaining to your leaving HEFA. These were all occasions which you felt were personal in nature, and therefore you paid personally.

In contrast, on those occasions where you entertained Wolfe for business purposes, you paid using

HEFA funds. For example, in 1991 during a conference in Mystic, Connecticut, you through HEFA hosted a dinner for a number of HEFA individuals and others, including Wolfe. This was a *business-related* social gathering because HEFA board members and other staff were present and the function provided a networking atmosphere for HEFA. You differentiate this type of event from the dinners which included only Wolfe, you and your spouses, which were of a social/personal nature.

You would not call Wolfe a "best friend." You encounter a number of people in your line of work. You tend to keep boundaries for business contacts. You considered Wolfe somewhat of a close friend because you felt that you could call on Wolfe for personal matters, if the opportunity arose.

II. **Discussion**

Section 3(b):

As the HEFA executive director, you were a state employee.[6/] As such, you were subject to the conflict of interest law, G.L. c. 268A.

Your receiving approximately $630 in entertainment from Wolfe raises issues under G.L. c. 268A, §3(b). Section 3(b) prohibits a state employee, otherwise than as provided by law for the proper discharge of official duty, from directly or indirectly, receiving anything of substantial value for himself for or because of any official act or act within his official responsibility[7/] performed or to be performed by him. Anything with a value of $50 or more is of substantial value for §3 purposes.[8/] You made decisions and took actions regarding what items would go on the HEFA board's agenda, which staff would be assigned to a bond proposal, the negotiation of bond pricing, and the choice of a manager for a pool or a short-term investment manager for bond proceeds. Each of those decisions and actions were official acts or acts within your official responsibility performed or to be performed by you. Moreover, you had the authority to intervene at any time in the acts of your staff which involved the evaluation, presentation and/or consideration of various bonding, underwriting and contractual issues either at the staff or board level. This authority, when exercised, involved official acts or acts within your official responsibility performed or to be performed by you. Goldman Sachs had a significant financial interest in how you performed or would perform these official acts because the acts did or could impact on its business interests. There is no compelling evidence of friendship or a private business relationship to justify the gratuities that you received from Wolfe.[9/] Therefore, while there is no evidence of a *quid pro quo*,[10/] there is reasonable cause to believe that your acceptance of the above free meals and tickets of substantial value was for or because of official acts or acts within your official responsibility performed or to be performed by you, and that you thereby violated §3(b).

Section 23(b)(3)

The above conduct also raises an appearance issue under G.L. c. 268A, §23(b)(3). Section 23(b)(3) prohibits a state employee from knowingly or with reason to know acting in a manner which would cause a reasonable person knowing all of the facts to conclude that anyone can...unduly enjoy his favor in the performance of his official duties.[11/]

When you accepted the $630 in entertainment from Wolfe, you knew (1) that he was an employee of Goldman Sachs, and (2) that Goldman Sachs, as a leading underwriter of HEFA bonds, had an interest in business dealings with HEFA. Thus, in the Commission's view, your acceptance of such gratuities while you were acting as HEFA's executive director on matters of interest to Goldman Sachs constitutes acting in a manner which would cause a reasonable person to conclude that Goldman Sachs could unduly enjoy your favor in the performance of your official duties.[12/] This is so even though you and Wolfe appear not to have discussed business during the events in question, and even though there is no evidence to indicate that you were ever unduly influenced in the performance of your official duties to favor Goldman Sachs' interest. Ultimately, accepting such entertainment under these circumstances creates an appearance of undue influence. Therefore, there is reasonable cause to believe that you violated §23(b)(3).[13/]

Mitigating Circumstances

The Commission recognizes that its long line of §3 precedent has primarily dealt with employees of regulatory, policy-making or adjudicative agencies, such as legislators, municipal treasurers and inspectors. In those contexts, the Commission's precedent is clear that the receipt of gratuities by a regulator from a regulatee with whom he has official dealings violates chapter 268A.

Certain state agencies, however, such as HEFA, are different from state regulatory bodies in that they operate more like private businesses than government agencies. In effect, they have to compete for clients in order to exist. For example, HEFA must compete with MIFA for many clients, as well as possible private funding sources. Additionally, HEFA bonds must compete for buyers in the financial marketplace with a host of other offerings. Also, as discussed above, all of HEFA's funding is derived from the fees it charges its clients like a private business. And it is run by a board of directors, much like a private corporation. Because it is financed and run more like a private business than a state agency, we describe it here as "quasi-private".

The Commission has not clearly addressed the application of chapter 268A, §3 to employees of "quasi-private" independent authorities such as HEFA. Consequently, employees of these agencies may have misperceived how the Commission's §3 precedent applies to them. The Commission takes this opportunity to make clear that even though the employees of these agencies operate almost continually in a business environment, they are nevertheless state employees and, therefore, must abide by chapter 268A. As with all public employees, employees of "quasi-private" agencies are prohibited from accepting gratuities of substantial value from persons or entities with whom they have official dealings, even if these are not traditional regulatory dealings, absent a legitimate motive unrelated to their official duties such as a private business or friendship relationship.

Although there is evidence of a friendly relationship between you and Wolfe, your receipt of these gratuities appears to have been motivated at least in part by your business relationship and, more particularly, acts which you were authorized to take as HEFA executive director. Thus, this is a case of mixed motive which, although not a defense, provides some mitigation when compared to a situation where the *sole* reason the gratuity is accepted is for or because of official acts or acts within one's official responsibility.

Your reciprocating by personally paying for certain dinners and events is further justification for this mixed motive conclusion. In other words, your reciprocating is additional evidence of friendship. It further distinguishes your situation from one in which no reciprocation occurs. Here, however, even when the degree of reciprocation is considered with the other evidence, friendship does not appear to be *the* motive for these gratuities.

More importantly, even if you did reciprocate dollar for dollar, c. 268A, §3(b) does not permit public officials to accept items of substantial value so long as they later reciprocate, although again it is arguably somewhat of a mitigating factor when compared to a situation without reciprocation.

III. **<u>Disposition</u>**

Based on its review of this matter, the Commission has determined that the sending of this letter should be sufficient to ensure your understanding of, and your future compliance with, the conflict of interest law.

The Commission is authorized to impose a civil penalty of up to $2,000 for each violation of c. 268A. Arguably, your substantive violations may be viewed in the context of the quasi-private business nature of HEFA's activities and the fact that a friendship developed between you and Wolfe in which you reciprocated for some of the gratuities received. For these reasons the Commission has decided to resolve your situation with a public enforcement letter and not by authorizing an adjudicatory proceeding in which it could impose a civil penalty. Another reason for the Commission to address your situation with a public enforcement letter is that it gives the Commission an opportunity to make clear that reciprocation, under these circumstances, is not a defense to a §3 violation.

In resolving your situation with a public enforcement letter the Commission does not mean to suggest that public employees of a so-called quasi-private agency such as HEFA who have accepted illegal gratuities prior to the date of this letter would also receive such a resolution if they came before the Commission. The resolution of this case was a function of *all* the factors enumerated above. Obviously, as to conduct occurring after the date of this letter, the fact that the subject is an employee of such an agency would have no bearing on the resolution.

This matter is now closed.

DATE: June 19, 1997

[1]Boston City and Winthrop Hospitals received federal HUD financing during or shortly before your tenure.

[2]*See Opinion of the Justices*, 354 Mass. 779, 784-785 (1968) (Senate No. 689, a bill leading to St. 1968, c. 614, constitutional because it involves no public money and no loan of public credit).

[3]Negotiating the bond pricing would typically involve a series of conference calls with the underwriter(s) and others to try to arrive at the lowest interest rate at which the bond issue could be reliably sold in the marketplace.

[4]Wolfe left Goldman Sachs in May 1995.

[5]According to you, by July 1990 you had developed a sufficiently close relationship with Wolfe that you and he would regularly go out for a social drink after a business meeting; his daughter would frequently appear at your office to see her father socially; and you and Wolfe would often arrange to meet at bond conferences or other bond industry meetings.

[6]G.L. c. 268A, §1(q) defines "state employee" as "a person performing services for or holding an office, position, employment, or membership in a state agency...."

G.L. c. 268A, §1(p) defines "state agency" as "any department of a state government including the executive, legislative or judicial, and all councils thereof and thereunder, and any division, board, bureau, commission, institution, tribunal or other instrumentality within such department, and *any independent state authority* [emphasis added], district, commission, instrumentality or agency, but not an agency of a county, city or town."

[7]G.L. c. 268A, §1(p) defines "official responsibility" as "the direct administrative or operating authority, whether intermediate or final, and either exercisable alone or with others, and whether personal or through subordinates, to approve, disapprove or otherwise direct agency action."

[8]*See Commonwealth v. Famigletti*, 4 Mass. App. 584 (1976); *EC-COI-93-14*.

[9]Friendship is not a defense to a §3 violation unless it is *the* motivating factor. *Scaccia*, 1996 SEC 838, 850, n. 27. Here that was not the case.

[10]In determining whether the items of substantial value have been given for or because of official acts within one's official responsibility, it is unnecessary to prove that the gratuities given were generated by some specific identifiable act performed or to be performed. *United States v. Sawyer*, 85 F. 3d 713, 730 (1st Cir. 1996); *Scaccia*, 1996 SEC 838, 844.

[11]Section 23(b)(3) goes on to provide, "It shall be unreasonable to so conclude if such officer or employee has disclosed in writing to his appointing authority or, if no appointing authority exists, discloses in a manner which is public in nature, the facts which would otherwise lead to such conclusion."

[12]This conclusion would apply even if, in fact, the motive for the entertainment was friendship because a concern would always remain that you might have been influenced by the gratuities to favor Goldman Sachs. Indeed, the Commission has stated that friendship only serves to enhance the appearance of favoritism that arises when a public official accepts items of substantial value from a member of the private sector over which the public official can have official impact. *Keverian*, 1990 SEC 460.

[13]You could have dispelled any such appearance of conflict by making a written disclosure pursuant to §23(b)(3).